Statement by Governor - Fourth Bi-monthly Monetary Policy Statement, 2019-20, October 4, 2019

Over the past three days, *i.e.*, during 1st, 3rd and 4th October, 2019 the Monetary Policy Committee discussed and evaluated recent macroeconomic and financial developments, and the outlook. Taking into consideration all available information and analyses, the MPC voted unanimously to reduce the policy repo rate, with five members voting to reduce the policy rate by 25 basis points. The MPC also decided to continue with the accommodative stance as long as it is necessary to revive growth, while ensuring that inflation remains within the target.

2. I would like to express my gratitude to the MPC members for the discussions we had, and their deep insights and experience, which are reflected in the policy decision and in the Resolution that has just been released on the website of the RBI.

3. I also want to thank our teams in the RBI for their continued high quality support to the MPC's deliberations with their hard work, research and logistics.

4. Let me begin by giving a brief overview of the salient aspects of the MPC's deliberations. In its view, the global economy has lost further momentum since the August 2019 meeting of the MPC, with trade and geo-political tensions purveying heightened uncertainty. Among advanced economies (AEs), the slowdown in the second quarter of calendar 2019 appears to have extended into the third quarter as well. For emerging market economies (EMEs), the worsening global economic and trade environment is weighing upon their macroeconomic performance. Crude oil prices were pulled down by softer demand and adequate supplies until the mid-September disruptions in refineries in Saudi Arabia, but normalisation has occurred faster than expected. Global financial markets have remained unsettled, with bouts of volatility in response to pessimism over global growth prospects. Against this backdrop,

central banks across the world are becoming increasingly accommodative in their monetary policy stances, aided by benign inflation conditions.

5. With regard to the domestic economy, the slump in real GDP growth to 5 per cent in the first quarter of 2019-20 has been followed by generally weaker high frequency indicators for the second quarter. Industrial production was lower in July 2019 on a year-on-year basis, pulled down mainly by manufacturing. The production of capital goods and consumer durables contracted. The output of eight core industries contracted in August, with the production of coal, electricity, crude oil and cement decelerating or going into contraction. The manufacturing PMI for September 2019 was flat, though still in the expansion zone. High frequency indicators suggest that services sector activity weakened in July-August. Indicators of rural and urban demand continued to slow down in July-August. The Reserve Bank's consumer confidence survey also shows weak consumer sentiment, especially relating to non-essential items.

6. On the positive side, there has been a rapid catch-up in the south-west monsoon rainfall, after an initial delay in its onset. By September 30, 2019, the cumulative all-India rainfall surpassed the long period average (LPA) by 10 per cent. While the first advance estimates of major kharif crops for 2019-20 are only 0.8 per cent lower than last year's fourth advance estimates, the prospects for the *rabi* 2019 season have brightened, with the live storage of water in major reservoirs on September 26, 2019 being 115 per cent of the live storage of the corresponding period of the previous year and 121 per cent of average storage level over the last ten years. Abundant rains in August and September have led to improved soil moisture conditions in most parts of the country. Overall, Indian agriculture is well-positioned to lead the recovery, which augurs well for rural employment and income, and the revival of domestic demand. In the industrial sector, consumer non-durables and intermediate goods have posted sustained expansion during 2019-20 so far and have emerged as potential growth drivers. Moreover, the infrastructure/construction sector activity look better in August,

as per the IIP data. Among service sector indicators, domestic air passenger traffic accelerated in August.

7. Turning to the external sector, with merchandise imports contracting faster than exports, the trade deficit narrowed during July-August, 2019. Higher net services receipts and private transfer receipts helped contain the current account deficit to 2.0 per cent of GDP in Q1:2019-20 from 2.3 per cent a year ago. On the financing side, net foreign direct investment rose to US$ 17.7 billion in April-July 2019 from US$ 11.4 billion a year ago. Net foreign portfolio investment (excluding the voluntary retention route) was of the order of US$ 3.3 billion during April-September 2019 as against net outflow of US$ 11.5 billion in the same period of last year. Net disbursals of external commercial borrowings rose to US$ 8.2 billion during April-August 2019 as against net repayments of US$ 0.2 billion during the same period a year ago. India's foreign exchange reserves were at US$ 434.6 billion on October 1, 2019 – an increase of US$ 21.7 billion over end-March 2019.

8. On the inflation front too, there have been positive developments. Consumer price headline inflation has moved in a narrow range of 3.1-3.2 per cent between June and August. While food inflation picked up, fuel prices moved into deflation; and inflation excluding food and fuel softened in a broad-based manner in August, and offset the firming up of food prices. Inflation expectations of households rose by 20 basis points for the one year ahead horizon, but this possibly reflected households' adaptive expectations in response to the rise in food prices in recent months. Manufacturing firms see weak pricing power in Q3, which renders the outlook for selling prices benign.

9. Overall liquidity in the system remained in surplus in August and September. Reflecting easy liquidity conditions, the weighted average call rate (WACR) traded below the policy repo rate in August and September. However, monetary transmission remains work in progress. As against the cumulative policy repo rate reduction of 110 bps during February-August 2019, the

weighted average lending rate (WALR) on fresh rupee loans of commercial banks declined by 29 bps.

10 Taking into account these developments, and the impact of recent policy rate cuts, the MPC has revised CPI inflation projections slightly upwards to 3.4 per cent for Q2:2019-20, but retained its projections for H2:2019-20 at 3.5-3.7 per cent. For Q1:2020-21, inflation is projected at 3.6 per cent, with risks evenly balanced. Real GDP growth for 2019-20 has now been revised downwards from 6.9 per cent in the August policy to 6.1 per cent – 5.3 per cent in Q2:2019-20 and in the range of 6.6-7.2 per cent for H2:2019-20 – with risks evenly balanced; GDP growth for Q1:2020-21 has also been revised downwards to 7.2 per cent.

11. Noting that the output gap has widened since its last meeting, the MPC was of the view that the continuing slowdown warrants intensified efforts to restore the growth momentum. Recent measures announced by the Government are likely to help strengthen private consumption and spur private investment activity. With policy space available on account of inflation expected to remain below target in the remaining period of 2019-20 and Q1:2020-21, the MPC decided to reduce the policy rate by 25 basis points and continue with the accommodative stance as long as it is necessary to revive growth, while ensuring that inflation remains within the target.

12. Now, I shall address some developmental and regulatory policy measures undertaken today for strengthening regulation and supervision; broadening and deepening financial markets; and improving the payment and settlement systems.

13. On regulation and supervision, micro finance institutions (MFIs) play an important role in delivering credit to those in the bottom of the economic pyramid. Accordingly, the household income limit for borrowers of Non-Banking Financial Company-Micro Finance Institution (NBFC-MFIs) has been increased from the current level of ₹1.00 lakh for rural areas and ₹1.60 lakh for urban/semi urban areas to ₹1.25 lakh and ₹2.00 lakh, respectively.

Furthermore, the lending limit per eligible borrower has been raised from ₹1 lakh to ₹1.25 lakh. These measures are expected to boost MFI lendings to the bottom of the economic pyramid.

14. In the area of financial markets, some of the recommendations of the Task Force on Offshore Rupee Markets (Chairperson: Smt. Usha Thorat) have been accepted. Accordingly, domestic banks will be allowed to freely offer foreign exchange prices to non-residents at all times, out of their Indian books, either by a domestic sales team or through their overseas branches. Also, rupee derivatives (with settlement in foreign currency) will be allowed to be traded in International Financial Services Centres (IFSCs). Other recommendations of the Committee are under consideration.

15. The scope of non-interest bearing Special Non-resident Rupee (SNRR) Account has been expanded by permitting persons resident outside India to open such accounts to facilitate rupee denominated external commercial borrowing (ECB), trade credit and trade invoicing. Furthermore, restriction on the tenure of SNRR accounts, which is currently 7 years, will also be removed for these purposes.

16. On payment and settlement systems, several measures have been announced. First, collateralised liquidity support, which is currently available till 7.45 pm, will now be available round the clock on all NEFT working days in order to facilitate smooth settlement of National Electronic Funds Transfer on 24x7 basis for members of public from December, 2019. This will help in better funds management by banks. Second, in order to strengthen the grievance redressal mechanism for customer complaints, it has been decided to institutionalise an internal ombudsman scheme at the large non-bank pre-paid payment instruments (PPI) issuers (entities who have more than 10 million pre-paid payment instruments outstanding). Third, in order to increase digitisation in Tier III to Tier VI centres through wider acceptance infrastructure, and as indicated in the Payment System Vision Document 2021 of RBI and also recommended

by the Committee on Deepening of Digital Payments (Chairperson: Shri Nandan Nilekani), it has been decided to create an Acceptance Development Fund (ADF). Fourth, with a view to expanding and deepening the digital payments ecosystem, it has been decided that State/UT Level Bankers Committees (SLBCs/ UTLBCs) shall identify one district per State/UT on a pilot basis in consultation with banks and stakeholders to make it 100% digitally enabled. The identified district may be allocated to a bank with significant footprint in that district. This would enable every individual in the pilot district to make/receive payments digitally in a safe, secure, quick, affordable and convenient manner.

Thank you.